Churchill Management Group

Monthly Market Update

August 11, 2020

TACTICAL STRATEGIES

PREMIER WEALTH TACTICAL & PREMIER WEALTH TACTICAL CORE

Despite the lingering COVID shutdown, stocks continued to grind higher in July. It was the fourth month of gains in a row, with August off to a positive start for the indices as well.

Markets were led by the same popular mega cap names, such as Apple and Amazon, though they were joined by the small caps last week. Small caps and midcaps jumped out to a strong start last week, notching gains of 6% and 5%, respectively.

While many companies have been challenged in the COVID environment, the large technology companies have seemed to thrive. Earnings reports from Amazon, Apple, Facebook, Microsoft, Netflix, and others showed the group flourishing with impressive revenue and earnings gains. Maybe we only need our computers to be at home and Amazon to deliver our goods. Smaller caps had been lagging in this environment, likely because larger companies tend to have stronger balance sheets and better access to capital, which increases their ability to weather the storm.

Even within the S&P 500, we have seen a distinct performance advantage for the larger market capitalization stocks. The largest ten percent of companies in the S&P by market cap are up 8.22% for the year, while the bottom ten percent are down a whopping 37.5%. On average, the second-, third-, and fourth-lowest deciles are down 16%, 11% and 8%, respectively. In this market, there has clearly been an edge based on size.

With earnings season mostly over, we saw a trend with companies beating what had been low expectations. Companies beat estimates 84% of the time, the highest rate in history. While that sounds great, the other side of coin is that the bar was set low due to the uncertainty of the coronavirus crisis and the lack of guidance from companies.

Yet, even with some improvement in earnings, it appears that stock prices may be outrunning even optimistic 12-month forward earnings hopes. The forward P/E ratio has risen to 22 times, a level last seen only in the dot-com bubble. While this remains a major concern, we are also aware that valuations can rise even further, especially when factoring in the possibility of a bubble driven by trillions in stimulus spending.

The economic challenges in the near term are daunting, but for now, stock markets appear to be looking beyond the current environment. Without question, stimulus efforts from both the monetary and fiscal authorities have played a major role in the market's recovery. The Fed has kept interest rates at historic lows and stimulus checks have kept incomes higher than normal for those unemployed. Congress is debating over another round of stimulus and the Federal Reserve has stated explicitly that they are prepared to provide more support as needed, with the view that any contraction of monetary policy is likely years away. To date, one would have to say the Fed's actions have, at least, kept the market elevated even if the economy has years of work ahead of it.

The technical action in July was encouraging. The Nasdaq hit all-time highs, while the S&P 500 is an eyelash away from a new record. Many stocks that had technical breakouts were able to follow through, though many are extended.

In our tactical strategies, we have remained cautious given the fundamentals behind the rally. For careful investors, this market is somewhat challenging as the rally sometimes defies logic. It is not completely unusual for the market to behave this way. We have taken small steps to increase exposure recently as the Dow and S&P 500 were able to break out after consolidating for the last couple of months. We will continue to adjust our exposure levels as appropriate. If the optimistic scenario materializes and our indicators turn more positive, we will continue to add exposure. On the other hand, if the current market optimism is misplaced and it turns out this is ultimately just a part of a long topping process, we can always pare back. In the meantime, our fully invested strategies have been getting their share from the market rallies (see below for additional information).

TACTICAL OPPORTUNITY

Up some 20% since July 1, Apple has led the tech-driven rally with a huge surge. Amazon also posted a stellar month in July, although gains were less than half those of Apple. Yet, buy signals remain a bit scarce outside of the big leaders, with fewer stocks meeting our model's criteria and many already extended. We have seen some lag from a few health-related names in the portfolio, but they remain holds for now.

FULLY INVESTED

ETF SECTOR ROTATION

Behind the lift of a frothy market, all eleven sectors in the S&P were up in July. The only significant laggard was Energy. During July, we remained in a mixed bag of weightings between the growth oriented Tech (Apple, Microsoft), Discretionary (Amazon) and Communications (Google, Facebook) sectors combined with the more defensive Consumer Staples and Healthcare. Last month the growth group was better than the defensives.

Industrials was the top sector, led by a big jump in UPS over the last few weeks – someone must deliver all those Amazon packages.

Small Caps behaved well in the last few weeks, especially on the Value side, but no buy signal yet. Growth was as good or better for Mid Caps and Large Caps. We remain in Large Cap Growth and Mid Cap Growth for broad market choices.

On the international front, Emerging Markets moved along with U.S. Markets, while Europe lagged. We have a position in Emerging Markets and no position in the European sphere.

EQUITY GROWTH AND VALUE

We saw good gains from the big names as the large players keep getting larger. Apple, Facebook, Amazon, Thermo Fisher Scientific, and Nvidia have all made nice gains. We have done some rotating to reduce exposure in certain stocks because of increased profits – a nice problem to have. However, so far, the leaders continue to grow.

EQUITY GROWTH OPPORTUNITY

July was another good month for the strategy. We saw bouts of rotation out of the high flying stay at home technology plays and decided to take some profits in this area. Big gainers Zoom and Fastly were sold after they had a great run. We are keeping a watchful eye on the composition of the portfolio as we are seeing more profit taking out of the leading technology sector. We remain comfortable with our remaining overweight in technology at this point.

EQUITY DIVIDEND INCOME

For the most part, dividend stocks rode the wave up, although not as strongly as the tech-heavy indices. Target, Kimberly-Clark and Pfizer posted strong gains. UPS and Qualcomm also delivered big jumps. As we continue to weed the portfolios, we are currently underweight Financials and Energy compared to most dividend indices. We will keep an eye out for any rotation in that regard.

For a full description of each strategy, please click here.

Best regards,

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